Supreme Court, U.S.
FILED
OCT 17 1991
OFFICE OF THE CLERK

No. 91-381

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

THE PEOPLE OF THE STATE OF ILLINOIS *EX REL.* THE OFFICE OF PUBLIC COUNSEL,
Petitioner,

v.

THE ILLINOIS COMMERCE COMMISSION, *et al.,*
Respondents.

Petition For Writ Of Certiorari To The Illinois Supreme Court

BRIEF OF RESPONDENT ILLINOIS COMMERCE COMMISSION IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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Printed by Authority of the State of Illinois (P.O. 35241—125—10-17-91)

QUESTION PRESENTED

Whether the Illinois Supreme court correctly held that Congress' enactment of the Natural Gas Act, 15 U.S.C., § 717 *et seq.* (1987), precludes state regulatory commissions from conducting prudency reviews regarding the pass-through to end-use customers, of direct-billed take-or-pay costs imposed upon local distribution companies by the Federal Energy Regulatory Commission ("FERC").

TABLE OF CONTENTS

	PAGE
QUESTION PRESENTED	i
TABLE OF AUTHORITIES	iii
CONSTITUTIONAL PROVISION AND STATUTE INVOLVED	2
STATEMENT OF THE CASE	3
SUMMARY OF THE ARGUMENT	10
REASONS FOR DENYING THE WRIT	11
I.	
STATE AGENCIES ARE PREEMPTED BY BOTH THE SUPREMACY CLAUSE AND THE FILED RATE DOCTRINE FROM REVIEWING THE PRUDENCY OF FERC-ALLOCATED, DIRECT-BILLED TAKE-OR-PAY COSTS	12
A. The take-or-pay liabilities involved in this case are FERC-mandated	15
B. The law of preemption is directly applicable to the take-or-pay costs involved in this case	16
C. Congress intended to preempt this area as it involves the rates, charges and allocations of costs associated with providing sales for resale services	18
II.	
THE FILED RATE DOCTRINE IS A RULE DESIGNED TO ENFORCE THE SUPREMACY CLAUSE OF THE CONSTITUTION, IT IS NOT A RULE OF DEFERENCE TO THE DECISIONS OF ADMINISTRATIVE AGENCIES	21
CONCLUSION	22

TABLE OF AUTHORITIES

Cases	PAGE
Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571, 169 L.Ed. 856, 101 S.Ct. 2925 (1981)	14
City of Chicago v. Illinois Commerce Commission, 13 Ill. 2d 602 (1958)	3, 13, 15
FPC v. Southern California Edison Co., 376 U.S. 205, 11 L.Ed. 2d 638, 84 S.Ct. 644 (1964) ..	13, 21, 22
General Motors Corporation v. Illinois Commerce Commission, 143 Ill. 2d 407 (1991)	9, 10, 11, 21
General Motors Corporation v. Illinois Commerce Commission, 191 Ill. App. 3d 450 (1990) ...	8, 9, 21
Interstate Natural Gas Co. v. Federal Power Commission, 331 U.S. 682 (1947)	19
Kentucky West Virginia Gas Company v. Pennsylvania Public Utility Commission, 837 F.2d 600 (3rd Cir. 1988)	16, 17
Mississippi Power & Light Co. v. Moore, 487 U.S. 354, 101 L.Ed 2d 322, 108 S.Ct. 2428 (1988)	3, 7, 12, 14, 17, 18, 20
Mississippi River Fuel Corporation v. Federal Power Commission, 121 F.2d 159 (1941)	19
Nantahala Power and Light Company v. Thornburg, 476 U.S. 953, 90 L.Ed 2d 943, 106 S.Ct. 2349 (1986)	3, 12, 13, 15, 20, 21
Public Utilities Commission of Ohio v. United Fuel Gas Company, 317 U.S. 456 (1943) ...	19
Re Costs Associated with Take-or-pay Charges, 95 PUR 4th 5 (1988)	3, 7
Re Costs Associated with Take-or-pay Charges, 97 PUR 4th 189 (1988)	3, 4, 7, 8

Other Authorities

The Supremacy Clause of the United States Constitution (U.S. Const., art. VI, cl. 2) 2

The Natural Gas Act, § 1(b), (15 U.S.C.A., § 717(b)) . 2

FERC Statutes and Regulations, Regulations Preambles (CCH), ¶ 30,637 (1985) 4

FERC Statutes and Regulations, Regulations Preambles (CCH), ¶ 30,665 (1985) 5

FERC Statutes and Regulations, Regulations Preambles (CCH), ¶ 30,761 (1987) ..... *passim*

FERC Statutes and Regulations, Regulations Preambles (CCH), ¶ 30,867 (1989) 9

Ill. Rev. Stat. 1987, ch. 111⅔, § 9-220 ..... 8, 18

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CONSTITUTIONAL PROVISION AND STATUTE INVOLVED

The Supremacy Clause of the United States Constitution (U.S. Const., art. VI, cl. 2):

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

The Natural Gas Act, § 1(b), (15 U.S.C.A., §717(b)):

> (b) The provisions of this Chapter shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

STATEMENT OF THE CASE

On November 22, 1988, the Illinois Commerce Commission ("Commission") entered an order in Commission Docket No. 88-103 establishing the preferred methodology for Local Distribution Company ("LDC") recovery of "take-or-pay" settlement costs billed to them by interstate pipeline companies. *Re Costs Associated with Take-or-pay Charges*, 97 PUR 4th 189 (1988) ("November Order"). In an earlier interim order in this matter concerning the scope of the hearing, the Commission found, *inter alia*, that the "filed rate doctrine" should be applied in the investigation. The filed rate doctrine is a rule of preemption, which requires states to give effect to wholesale rates on file with or approved by the FERC. The Commission found that the filed rate doctrine requires that it permit the recovery of all take-or-pay costs incurred through FERC-approved direct-billed rates. *Re Costs Associated with Take-or-pay Charges*, 95 PUR 4th 5 at 9 (1988), citing *Mississippi Power & Light Co. v. Moore*, 487 U.S. 354, 101 L.Ed 2d 322, 108 S.Ct 2428 (1988); *Nantahala Power and Light Company v. Thornburg*, 476 U.S. 953, 90 L.Ed 2d 943, 106 S.Ct. 2349 (1986); *City of Chicago v. Illinois Commerce Commission*, 13 Ill. 2d 602 (1958).

Take-or-pay clauses are a standard and accepted part of long-term gas purchase agreements between interstate pipelines and their producer-suppliers. The FERC noted in a 1985 policy statement that:

> Contracts for the sale of natural gas have traditionally contained provisions requiring the purchaser to take, or pay for, if tendered by the seller and not taken, some specified quantity of natural gas. (footnote omitted) Typically, the contracts provided for a specified period during which gas paid for could be

> "made up" by the buyer. Indeed, during the 1960's, following a period during which a number of pipelines experienced take-or-pay difficulties, the Commission promulgated a rule in effect requiring a five-year period for jurisdictional sales.

Regulatory Treatment of Payments Made in Lieu of Take-or-pay Obligations, FERC Statutes and Regulations, Regulations Preambles (CCH), ¶ 30,637, p. 31,301 (1985).

Under take-or-pay agreements, pipelines are required to pay for a stated volume of natural gas held by a producer, whether or not that quantity is actually taken by the pipeline in order to serve LDCs. As the Commission noted in its November Order, pipeline take-or-pay problems developed when pipelines were no longer able to maintain historical levels of gas purchases in order to avoid the take-or-pay liability as specified in their contracts with producers. *Re Costs Associated with Take-or-pay Charges*, 97 PUR 4th 189, 192 (1988).

In its November Order, the Commission described four historical events which appear to have caused the take-or-pay problem. First, a nationwide shortage of natural gas took place in the 1970's resulting in many LDCs having to curtail sales of natural gas to end-use customers. Second, as a result of this shortage of natural gas, interstate pipelines sought out new sources of gas and contracted for substantial volumes of new natural gas from producers. Third, in response to the national shortage of natural gas which was occurring, Congress enacted the Natural Gas Policy Act of 1978, resulting in additional sources of natural gas becoming available, but at higher prices than had been previously charged. Finally, a "gas bubble" or surplus developed which gave rise to the spot gas market which further eroded the market for pipeline sales gas. The foregoing events and factors combined to

reduce the pipelines' need to take long term gas supplies from producers. The reduced market for pipeline sales gas led in turn to the take-or-pay problem.

In reaction to these market forces, new supplies of natural gas developed, creating a surplus which allowed both LDCs and large end-use customers of LDCs to by-pass interstate pipelines and their suppliers, and purchase natural gas directly from sellers at lower prices on the "spot market." Consequently interstate pipelines saw their take-or-pay liabilities increase as a result of their inability to sell contracted supplies of gas to LDCs.

In response to these developments in the natural gas industry, the FERC issued its Order No. 436, on October 9, 1985. FERC Statutes and Regulations, Regulations Preambles 1982-1985 (CCH), ¶ 30,665 (1985). Order 436 created an open access policy which provided a simplified gas transportation program, allowing LDCs to transport gas over an interstate pipeline without using the pipelines as a wholesaler. The "open access" policy resulted in pipeline customers having greater access to lower cost spot market gas, as an alternative to taking higher priced gas which pipelines had already contracted for with their suppliers. While both LDCs and their customers enjoyed the benefits of lower cost alternative sources of gas, pipeline take-or-pay liability increased because previously contracted gas was not being taken.

On August 7, 1987, the FERC issued its Order 500 dealing with the recovery of take-or-pay liability. FERC Statutes and Regulations, Regulations Preambles 1986-1989 (CCH), ¶ 30,761 (1987). The FERC established two methods for interstate pipelines to pass through to their customers the take-or-pay liabilities. *Id.* at 30,784-85. The first method permitted pipelines to use commodity rate

treatment for all take-or-pay costs which the FERC found were prudently incurred. This method allowed pipelines an opportunity to recover 100% of their prudently incurred take-or-pay costs, by adding them to the cost of gas sold in the future. *Id.* at 30,786.

Under the second method of recovery, if a pipeline was willing to absorb between 25% and 50% of its take-or-pay settlement costs, the FERC would presume that an equal amount of take-or-pay settlement costs were prudently incurred and allow recovery of those amounts through direct-billed charges to the pipeline's sales customers. The pipeline's remaining take-or-pay costs were recoverable through a commodity surcharge, or a volumetric surcharge on pipeline throughput. *Id.* at 30,784-85.

The Commission order which is the subject of this appeal was concerned only with the Commission's power to examine LDC actions with respect to the second method: direct billed allocations of take-or-pay settlement costs. As the Commission noted in its November Order, pipelines have uniformly opted for Order 500's direct-billing method of recovery, even though this method guarantees that they will not recover all of their take-or-pay costs.

The direct-billing method, which tends to guarantee the recovery of a minimum of 50% of a pipeline's total take-or-pay settlement expense, was preferable for several reasons. First, the framework of Order 500 discouraged pipeline customers from initiating prudence challenges before the FERC by creating the presumption that direct-billed costs were prudently incurred. Moreover, any party which failed in its efforts to challenge the prudence of these costs was required to pay its allocated share of the actual costs the FERC found prudent. This amount could be twice the amount that the challenger would have paid

under the direct-billing methodology. FERC Statutes and Regulations, Regulations Preambles (CCH), ¶ 30,761 at 30,787-88.

FERC Order 500 further required that the costs recovered through direct-billed take-or-pay charges would be allocated among a pipeline's customers based on each customer's contribution to the pipeline's decline in sales before and after "open access" took effect. Customers who took advantage of the lower cost spot market supplies were assigned a higher take-or-pay obligation than those customers who purchased higher priced gas from pipelines with take-or-pay contracts. FERC Statutes and Regulations, Regulations Preambles (CCH), ¶ 30,761 at 30,784-85 (1987).

On July 20, 1988, the Commission issued an "Interim Order" in Commission Docket No. 88-103 finding that under the Supremacy Clause of the Constitution, most recently interpreted by this Court in *Mississippi Power & Light Co. v. Moore*, 487 U.S. 354, 101 L.Ed 2d 322, 108 S.Ct 2428 (1988), the Commission was precluded from conducting a prudency review of direct-billed take-or-pay allocations and that the FERC could not require or authorize such a prudence review by state agencies. *Regarding Costs Associated With Take-or-pay Charges*, 95 PUR 4th 5, 8-9 (1988).

On November 22, 1988, the Commission issued its second order in the docket dealing with the remaining issues presented. The Commission found that take-or-pay charges should be recovered from all classes of customers, including transportation customers, on a uniform volumetric basis. *Re Costs Associated with Take-or-pay Charges*, 97 PUR 4th 189, 197 (1988).

In reaching its decision on these points, the Commission concluded that assessing take-or-pay costs on a volumetric basis was the most accurate way of reflecting the underlying factors which brought about the existence of take-or-pay costs as well as the benefits received from using alternative sources of gas supply. *Re Costs Associated with Take-or-pay Charges*, 97 PUR 4th 189, 197 (1988). The Commission also concluded that the recovery of take-or-pay charges under the mechanism of the Uniform Purchase Gas Adjustment Clause ("UPGA"), allowed under § 9-220 of the Illinois Public Utilities Act, provided the most efficient and effective mechanism for recovering take-or-pay costs, and was a cost of gas under the Illinois Public Utilities Act and the Commission's regulations. *Re Costs Associated with Take-or-pay Charges*, 97 PUR 4th 189, 197-98 (1988). Ill. Rev. Stat. 1987, ch. 111⅔, § 9-220.

OPC appealed the decisions of the Commission to the appellate court. *General Motors Corporation et al. v. Illinois Commerce Commission et al.*, 191 Ill. App. 3d 450 (1990). OPC contended that the Commission was not preempted from reviewing and possibly preventing the pass-through of direct-billed take-or-pay costs. OPC asserted that the Commission should conduct a "prudence review" to determine whether those costs had been properly incurred by the LDCs. In a 2-to-1 decision entered on December 5, 1989, the appellate court reversed the Commission's order. In its opinion, the majority held that the preemption analysis turned on the FERC's intent to preclude state regulatory commissions from considering whether the charges in question should be recoverable in their entirety. Because the FERC had suggested that there should be an "equitable sharing" of take-or-pay costs among the entire industry, including the LDCs, and had

stated that state regulatory commissions were free to consider a variety of issues with respect to take-or-pay costs, the majority found no intent on the part of the FERC to compel the states to permit recovery of 100% of those costs by the LDCs. *General Motors Corporation et al. v. Illinois Commerce Commission et al.*, 191 Ill. App. 3d 450, 462 (1990).

The dissenting member of the appellate court panel found no authority for a Commission initiated prudence review of purchasing decisions made by the LDCs. Justice Lund found the FERC's allocation of take-or-pay costs to LDCs to be controlling:

> In our present case, the FERC has determined that take-or-pay power costs, incurred by interstate power suppliers, shall be passed on to the LDCs. The take-or-pay costs have, thus, been determined to be part of the wholesale cost of power by the FERC, and must be allowed by the State utility commissioners as reasonable operating expenses when setting retail prices.

General Motors Corporation et al. v. Illinois Commerce Commission et al., 191 Ill. App. 3d 450, 465 (1990).

Subsequent to the issuance of the appellate court's opinion in this case, the FERC issued its Order 500-H. FERC Order No. 500-H (Dec. 21, 1989), 54 Fed. Reg. 52344, 49 FERC Statutes and Regulations, Regulations Preambles (CCH), ¶ 30,867. In the order, the FERC stated that its decisions regarding take-or-pay allocations are not intended to preempt state review of take-or-pay liabilities incurred by LDCs.

The Illinois Supreme Court reversed the decision of the appellate court. *General Motors Corporation et al. v. Illinois Commerce Commission et al.*, 143 Ill. 2d 407 (1991).

The court found that any reliance on the FERC's intent was misplaced, and that it was Congress' intent in enacting the Natural Gas Act which was controlling. The court further held that the case at bar presented the "classic situation for application of the [filed-rate] doctrine," and held that the filed rate doctrine prohibited the Commission from conducting prudency reviews of direct-billed take-or-pay costs imposed upon local distribution companies by the FERC. *General Motors*, 143 Ill. 2d 407, 423-24.

SUMMARY OF THE ARGUMENT

State agencies are preempted by both the Supremacy Clause and the filed rate doctrine from reviewing the prudency of FERC-allocated, direct-billed take-or-pay costs. Congress' intent to preempt this area is clear. The direct-billed take-or-pay charges at issue in this case involve the rates, charges and allocations of costs associated with providing sales for resale services. These charges clearly fall within the parameters of the FERC's jurisdiction. Moreover, reliance on the intent of the FERC in support of the assertion that the direct-billed take-or-pay charges involved in this case are subject to state prudency reviews is misplaced. The filed rate doctrine is a rule designed to enforce the Supremacy Clause of the Constitution, it is not a rule of deference to the decisions of administrative agencies. It is the intent of Congress which is decisive. In this case, the Natural Gas Act, as interpreted by this Court in the filed rate doctrine, preempts state agencies from reviewing the prudency of these FERC-allocated, direct-billed take-or-pay costs.

REASONS FOR DENYING THE WRIT

The Commission believes that regardless of the intention of the FERC, Order 500 established a rate or charge for natural gas. Order 500 preempts state regulatory agencies, such as the Commission, from altering or denying the pass-through of such costs to LDC customers. The Illinois Supreme Court correctly affirmed the Commission's November Order. The court properly described the issue as being whether the Commission "is preempted from disallowing distributors full recovery, from their customers, of the FERC-*allocated* take-or-pay costs. *General Motors Corporation v. Illinois Commerce Commission*, 143 Ill. 2d 407 at 412 (emphasis added).

The question before this Court is not, as Petitioner argues, whether the Commission is preempted from conducting a prudence review with regard to *all* take-or-pay costs which flow to LDCs from interstate pipelines. Rather, the question is whether the Commission and the Illinois Supreme Court were correct in finding that the Commission was foreclosed from reviewing the prudence of LDC purchasing decisions with regard to direct-billed, FERC-allocated, take-or-pay costs. Petitioner's global arguments improperly expand the scope of review of the Commission's decision with regard to these direct-billed costs.

A reading of the Commission's November Order indicates that the Commission's preemption analysis was confined, both in the July 20, 1988 Interim Order and in the November Order, to recovery of direct-billed, FERC-allocated costs. In contrast, the OPC improperly focuses on the preemption of take-or-pay costs in general. The Commission urges this Court to view the issue at hand in the same narrow manner as did the Commission. The issue is simply whether the Commission can

deny LDC recovery of direct-billed take-or-pay charges based on a prudence review of the LDC's purchasing practices. The Commission respectfully submits that the involuntary nature of these direct-billed, FERC-allocated costs, takes them outside the sphere of exceptions to the filed rate doctrine.

The Illinois Supreme Court's decision is entirely consistent with this Court's decisions explaining and applying the "filed rate doctrine." See *Mississippi Power & Light Co. v. Moore*, 487 U.S. 354, 101 L.Ed 2d 322, 108 S.Ct 2428 (1988); *Nantahala Power and Light Company v. Thornburg*, 476 U.S. 953, 90 L.Ed 2d 943, 106 S.Ct. 2349 (1986). For the reasons stated below, the petition for a writ of certiorari should be denied.

I.

STATE AGENCIES ARE PREEMPTED BY BOTH THE SUPREMACY CLAUSE AND THE FILED RATE DOCTRINE FROM REVIEWING THE PRUDENCY OF FERC-ALLOCATED, DIRECT-BILLED TAKE-OR-PAY COSTS.

The preemptive effect of FERC-set allocations is well established and was affirmed by this Court in *Nantahala Power and Light Company v. Thornburg*, 476 U.S. 953, 90 L.Ed 2d 943, 106 S.Ct. 2349 (1986). In that case, the North Carolina Utility Commission had determined that a FERC-set allocation of low-cost Tennessee Valley Authority electric power was too low, resulting in higher electric rates for end-use customers. The North Carolina Commission decided that the company should be imputed to have received a higher allocation of low cost power for purposes of determining its intrastate rates. The North Carolina appellate and supreme courts affirmed that decision.

This Court reversed. Looking first to the filed rate doctrine, this Court stated that federal and state courts are prohibited from reviewing the reasonableness of rates under the jurisdiction of the FERC and its predecessor, the Federal Power Commission ("FPC"), *Nantahala Power & Light v. Thornburg*, 476 U.S. 953, 963-64; 90 L.Ed. 2d 943, 952-53, 106 S.Ct. 2d 2349 (1986). The Court recognized that the filed rate doctrine is not a rule of administrative law designed to ensure that courts respect administrative decisions; rather, it is a matter of the enforcement of the Supremacy Clause of the Constitution. *Nantahala*, 476 U.S. at 963, 90 L.Ed. 2d at 952. Citing the Illinois Supreme Court's decision in *City of Chicago v. Illinois Commerce Commission*, 13 Ill. 2d 607 (1958) with approval, this Court noted that state courts had broadly applied the filed rate doctrine in several contexts where the FERC had established wholesale power prices. *Id.* at 965, 90 L.Ed. 2d at 953. In explaining the rationale behind its decisions and the decision of the various state courts, this Court stated that:

> [O]ur decisions have squarely rejected the view . . . that the scope of FPC jurisdiction over interstate sales of gas or electricity at wholesale is to be determined by a case-by-case analysis of the impact of state regulation upon the national interest. Rather, Congress meant to draw a bright line easily ascertained, between state and federal jurisdiction, making unnecessary such case-by-case analysis. This was done in the Power Act by making FPC jurisdiction plenary and extending it to all wholesale sales in interstate commerce except those which Congress has made explicitly subject to regulation by the States. *FPC v. Southern California Edison Co.*, 376 U.S. 205, 215-216, 11 L.Ed. 2d 638, 84 S.Ct. 644 (1964).

Id. at 966, 90 L.Ed. 2d at 954.

Thus, under the filed rate doctrine, as interpreted by this Court, state utility commissions are precluded from taking actions inconsistent with decisions made by the FERC within its regulatory authority. Specifically, the filed rate doctrine requires that States give effect to rates set by the FERC. *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571; 169 L.Ed. 856, 101 S.Ct. 2925 (1981).

This Court reaffirmed its view of the filed rate doctrine and the plenary authority granted the FERC in *Mississippi Power & Light v. Moore*, 487 U.S. 354, 101 L.Ed 2d 322, 108 S.Ct. 2428 (1988). In *Mississippi Power & Light*, this Court considered the extent of allowable state commission scrutiny over FERC-set payments by a retail utility to a wholesale utility regulated by the FERC. The Mississippi Supreme Court had held that the state commission erred when it allowed the recovery of the retail utility's FERC-allocated costs, without having first conducted its own review of the prudency of those costs.

In reversing the Mississippi Supreme Court's decision, this Court found that there was no room under the filed rate doctrine for the state commission to make its own determination of reasonable costs once those costs had been established by FERC:

> * * * States may not alter FERC-ordered allocations of power by substituting their own determinations of what would be just and fair. FERC-mandated allocations of power are binding on the States, and States must treat those allocations as fair and reasonable when determining retail rates.

Mississippi Power & Light, 487 U.S. 354, 371, 101 L.Ed. 2d 322, 338 (1988).

As discussed previously, prior to its decision in this case, the Illinois Supreme Court had also recognized the pre-

emptive effect the NGA has upon the Commission's ability to set natural gas rates in a case cited with approval by this court in *Nantahala*. *City of Chicago v. Illinois Commerce Commission*, 13 Ill. 2d 607 (1958); See *Nantahala*, 476 U.S. at 963, 90 L.Ed. 2d at 952. In *City of Chicago*, review of a Commission order was sought which allowed Peoples Gas Light and Coke Company, an Illinois LDC, to automatically adjust its rates to reflect changes in wholesale rates established by the FPC. The City of Chicago had contended that because Peoples Gas received its wholesale gas from two subsidiaries, the Commission was required to review the reasonableness of the Federal Power Commission-approved rates charged for that gas. The Illinois Supreme Court held that:

> [t]he Natural Gas Act of 1938, (Citation omitted) vested the power to fix rates for natural gas transported and sold to distributing companies in interstate commerce exclusively in the FPC and preempted any right which might have existed in the States to regulate such rates. (Citations omitted). [The Subsidiaries] must charge and Peoples must pay the FPC determined rate, and the Commission has no power over such rate.

City of Chicago v. Illinois Commerce Commission, 13 Ill. 2d 607, 614 (1958).

A. The take-or-pay liabilities involved in this case are FERC-mandated.

In an effort to circumvent this overwhelming authority, the OPC states that "[t]ake-or-pay liabilities are not FERC-approved allocations of costs or FERC-mandated payments." OPC Petition, p. 18. Rather, the OPC asserts, "the issue is intrastate and is tied to FERC only through the policy statements issued by the FERC directing the

states to allocate take-or-pay costs across all segments of the industry." *Id.* The OPC describes the Illinois Supreme Court's decision in this matter as being inconsistent with the preemption doctrine. None of the OPC's arguments are supportable or invite further judicial scrutiny.

OPC's assertion that direct-billed amounts allocated to an LDC and ordered to be paid by that LDC are neither an allocation of costs nor a mandated payment strains the imagination. It begs the question of whether the LDC has any choice to avoid the charge. The OPC has offered no theory of law which would indicate that once the FERC validly allocates a portion of an interstate pipeline's take-or-pay burden directly to a particular LDC that the LDC's payment of that allocated amount is either elective or avoidable.

B. The law of preemption is directly applicable to the take-or-pay costs involved in this case.

While the Commission agrees that states are only preempted by federal agency action in particular circumstances (see OPC Petition, p. 19), the Commission believes that the situation presented by this case is the precise situation contemplated by the filed rate doctrine. As the OPC recognizes, there are only three circumstances in which federal law may preempt state law. One of these is present here; where Congress has given a federal agency complete and plenary authority over an area of regulation. In such an instance, it is the intent of Congress, and not the interpretation of the agency, which must be given effect by the courts.

The Commission respectfully suggests that the case of *Kentucky West Virginia Gas Company v. Pennsylvania Public Utility Commission*, 837 F.2d 600 (3rd Cir. 1988)

demonstrates the proper purpose and focus of prudency reviews conducted by state commissions, as well as delineating the respective spheres of authority possessed by state and federal agencies. There, an LDC challenged the state commission's refusal to allow the recovery of the costs of gas purchased, based upon the conclusion that the utility was imprudent in not purchasing lower cost gas which was available at the time of purchase. The utility contended that because the cost of the higher cost gas was approved by FERC, the state commission was preempted from inquiring into its purchase decision. *Kentucky West Virginia Gas Company v. Pennsylvania Public Utility Commission*, 837 F.2d 600, 605.

The court rejected this contention, finding that while state commissions were clearly preempted from questioning or altering FERC rates which established the costs of gas, it was within the authority of the commission to inquire into, and deny the recovery of higher cost gas purchased, where other sources of lower cost gas were available. *Kentucky West Virginia Gas Company v. Pennsylvania Public Utility Commission*, 837 F.2d 600, 609.

This Court in *Mississippi Power & Light*, clearly recognized that the ability of a retail utility, such as an LDC, to exercise some choice in its purchase practices is the demarcation point between FERC authority under the filed rate doctrine, and that of a state commission operating under its own authority. This Court stated that:

> As we assumed [in *Nantahala*], it might well be unreasonable for a utility to purchase unnecessary quantities of high cost power, even at FERC-approved rates, *if it had the legal right to refuse to buy that power*. But if the integrity of FERC regulation is to be preserved, it obviously cannot be unreasonable for MP&L to procure the particular quantity of high-

> priced Grand Gulf power that FERC has ordered it to pay for. 101 L.Ed. 2d at 340. (Emphasis added).

Pursuant to § 9-220 of the Illinois Public Utilities Act, Ill. Rev. Stat. 1987, ch. 111⅔, § 9-220, annual reconciliation hearings take place at which time each Illinois LDC is required to establish the prudency of its purchase practices during the year under review. In order for this hearing to be meaningful in any sense, the prudency of a utility's purchase practices must focus only upon those costs concerning which the utility had the opportunity or choice to make a lower cost purchase.

The pass-through of take-or-pay costs in the present case, however, does not involve an issue or question of choice by the LDCs in their purchase practices. As distinct from the question of choice in gas purchases, the challenge made in this case is that some portion of the take-or-pay charges properly imposed on LDCs by the Order 500 allocation can be denied recovery from end-use customers. Such a challenge is clearly directed to the rate or charge imposed by FERC, and is prohibited by the filed rate doctrine, as set forth in *Mississippi Power & Light v. Moore*, 487 U.S. 354, 374, 101 L.Ed. 2d at 340.

C. Congress intended to preempt this area as it involves the rates, charges and allocations of costs associated with providing sales for resale services.

The OPC argues that the legislative history of the NGA shows that the Congress expressed no intent to preempt states in cases such as this, and that Congress did not intend to occupy the whole of natural gas regulation. OPC Petition, p. 20. These conclusions are purportedly gleaned from the fact that the Congress, in enacting the NGA, left certain admittedly interstate functions to state regula-

tion. For example, with regard to the interstate sale of gas, the Congress only chose to regulate sales for resale.

At the time the NGA was enacted, the states had been prohibited by the United States Supreme Court from regulating interstate pipelines because of the Commerce Clause. In enacting the NGA, the Congress intended to create a comprehensive scheme of regulation that would be complementary in its operation to that of the states, without any confusion of functions. *Public Utilities Commission of Ohio v. United Fuel Gas Company*, 317 U.S. 456 (1943). The chief purpose of the NGA was to secure regulation of the transporter and large scale seller in interstate commerce. *Mississippi River Fuel Corporation v. Federal Power Commission*, 121 F.2d 159 (1941).

The Natural Gas Act contemplated a dual system of regulation. The purpose of Congress in enacting the NGA was to occupy the field in cases where courts had found the states unable to act so that there would be no gaps in regulation. *See Interstate Natural Gas Co. v. Federal Power Commission*, 331 U.S. 682 (1947). Section 1 of the NGA enumerated the scope of the FERC's jurisdiction. Generally, federal regulation applies to the transportation of natural gas in interstate commerce but not to any other transportation. It applies to the sale in interstate commerce of natural gas for resale for ultimate public consumption but not to the local distribution of natural gas. The law in this regard is clear; the Commission is preempted from regulating interstate sales for resale. Thus, costs directly allocated to an LDC arising from pipeline maintenance of inventories to meet responsibilities for their sales for resale customers clearly fall outside the ambit of state regulation insofar as the LDC has no choice but to pay a specific allocated share of those costs.

To reiterate, the question is not whether the Congress intended to occupy the entire field of natural gas regulation but whether it intended to occupy the portions of the field at issue in this case, i.e., rates, charges and allocations of costs associated with providing sales for resale services. The law in this area, as established by this Court, amply demonstrates that Congress indeed intended to preempt the regulation of sales for resale. Take-or-pay charges are the direct result of pipeline cost of providing sales for resale services. The FERC has recognized as much by stating in Order 500 that:

> . . . It is true that the Commission's current policy, and one of the flowthrough mechanisms found acceptable in this rule, is that take-or-pay buyout and buydown costs are expenses related to the acquisition of gas supplies and should therefore be classified as production related and recovered through the pipeline's commodity rates.

FERC Statutes and Regulations, Regulations Preambles (CCH), ¶ 30,761, p. 30,786.

OPC's fixation on Congress' partial preemption of the entire natural gas field should not be allowed to obscure the fact that sales for resale and charges associated with those sales, are under the sole jurisdiction of the FERC.

States are not allowed to interfere with FERC's plenary authority over interstate wholesale rates. *Mississippi Power & Light Co. v. Moore*, 487 U.S. 354, 101 L.Ed 2d 322, 108 S.Ct. 2428 (1988); *Nantahala Power and Light Company v. Thornburg*, 476 U.S. 953, 90 L.Ed. 2d 943, 106 S.Ct. 2349 (1986). The lesson of these cases is clear: states are not allowed to "trap" costs found by the FERC to be reasonable, by denying LDC's the right to recover them from their ratepayers. To adopt the OPC's position could result in just such a "trapping" of costs. Therefore, OPC's assertions must be rejected.

II.

THE FILED RATE DOCTRINE IS A RULE DESIGNED TO ENFORCE THE SUPREMACY CLAUSE OF THE CONSTITUTION, IT IS NOT A RULE OF DEFERENCE TO THE DECISIONS OF ADMINISTRATIVE AGENCIES.

Finally, the OPC contends that the Illinois Supreme Court's decision in this matter is inconsistent with this Court's decisions which speak to a federal agency's power to declare its intention in the area of preemption. OPC Petition, pp. 38-43. OPC continues to place importance on the reasoning of the Illinois appellate court, which was rejected by the Illinois Supreme Court. See, *General Motors Corporation et al. v. Illinois Commerce Commission et al.*, 191 Ill. App. 3d 450, 462 (1990); *General Motors Corporation v. Illinois Commerce Commission*, 143 Ill. 2d 407, 421 (1991). Without inquiring into whether the FERC's interpretation was a correct one, the appellate court simply concluded that the FERC's interpretation was reasonable and followed it without further analysis.

By taking the FERC's opinion as to the effect of its orders at face value, the appellate court and the OPC misapprehend this Court's decision in *Nantahala*. Rather than treating the issue as one of enforcement of the Supremacy Clause, as required by *Nantahala*, the appellate court and the OPC relegate the filed rate doctrine to a rule of deference to the decisions of administrative agencies; the very rationale that was specifically rejected in *Nantahala*, 476 U.S. at 963, 90 L.Ed. 2d at 952. In addition, having ignored Congress' intent to give the FERC plenary authority in the field of natural gas rates, as interpreted by the courts in the filed rate doctrine, the court and the OPC engage in the very same case-by-case analysis this Court rejected in *FPC v. Southern California Edison*, 376 U.S. 205, 215-216, 11 L.Ed. 2d 638,

84 S.Ct. 644 (1964). A proper analysis of the preemption issue in this case cannot begin and end with the FERC's intent as expressed in its orders. It is the intent of Congress which is relevant, and in this case Congress intended to preclude state regulatory commissions from conducting prudency reviews regarding the pass-through to end-use customers of costs, such as these direct-billed take-or-pay costs, imposed upon local distribution companies by the FERC.

CONCLUSION

WHEREFORE, the Illinois Commerce Commission prays that this Court deny the petition for a writ of certiorari.

Respectfully submitted,

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